

SERVICE DATE - LATE RELEASE MAY 9, 2003

SURFACE TRANSPORTATION BOARD

DECISION

STB Finance Docket No. 34335

KEOKUK JUNCTION RAILWAY COMPANY-FEEDER LINE ACQUISITION-
LINE OF TOLEDO PEORIA AND WESTERN RAILWAY CORPORATION BETWEEN
LA HARPE AND HOLLIS, IL

Decided: May 9, 2003

On April 9, 2003, Keokuk Junction Railway Company (KJRY), a Class III railroad controlled by Pioneer RailCorp (Pioneer), filed an application under the Feeder Railroad Development Program. See 49 U.S.C. 10907 and 49 CFR Part 1151. KJRY seeks to acquire from Toledo, Peoria and Western Railway Corporation (TP&W) 76 miles of rail line between milepost 194.5 near La Harpe and milepost 118.5 at Hollis, IL, and the Mapleton Industrial Spur and Wye Facilities, a 2.5-mile connecting line near Hollis (the Line).¹

KJRY also filed discovery requests against TP&W as provided for by 49 CFR 1151.2(d). On April 24, 2003, TP&W filed a petition for leave to file a petition to reject, the petition to reject, and responses to KJRY's discovery requests. The United Transportation Union-Illinois Legislative Board filed a comment on May 5, 2003, in support of TP&W's petition to reject. KJRY filed a reply and a motion for a protective order on May 7, 2003.

Under 49 U.S.C. 10907(b)(1), the Board is authorized to require the sale of a rail line to a financially responsible person if the public convenience and necessity permit or require the sale. KJRY contends that the proposed sale is required under the public convenience and necessity criteria, 49 U.S.C. 10907(c)(1)(A)-(E), and that it is a financially responsible person willing to pay not less than the Line's constitutional minimum value. Under 49 U.S.C. 10907(b)(2), constitutional minimum value is defined as the greater of a line's net liquidation value (NLV) or going concern value (GCV). A financially responsible person is defined as a person able to pay the higher of a line's NLV or GCV and cover the expenses associated with providing rail service over the line for at least the first 3 years of operation. See 49 U.S.C. 10907(a).

¹ TP&W's ownership of the Line ends at Hollis. To reach the eastern portion of its system at East Peoria, TP&W operates trackage rights over Union Pacific Railroad Company between Hollis and Peoria and over Peoria and Pekin Union Railway Company between Peoria and East Peoria.

KJRY estimates that the Line has an NLV of \$3,393,363. KJRY's estimate relies on two lists of track materials that were prepared by TP&W as part of its earlier effort to sell off the bulk of the Line, the 71.5-mile segment between milepost 194.5 near La Harpe and milepost 123 in Peoria, IL (the West End).² The lists were analyzed in a study prepared for KJRY by Gohmann and Associates, Inc. (Gohmann), that assessed the NLV of the West End at \$3,088,833.³ In the study, the West End's rail, rail scrap, and other track material were valued at \$2,297,304; its ties were valued at \$343,308; and its ballast was valued at \$348,221. No values were assigned to the bridges, trestles, signals and other structures but the study observed that a bridge over a state highway might have to be removed and that this could reduce the West End's NLV by as much as \$500,000. The study also assumed marketable title to 50% of the land in the West End's right-of-way and valued it at \$100,000. Because the lists did not include data, and data were not otherwise available, for the 4.5-mile line segment between milepost 123 at Peoria and milepost 118.5 at Hollis and the 2.5-mile Mapleton Industrial Spur and Wye Facilities (together the Mapleton Segment), Gohmann derived an NLV of \$304,530 for the Mapleton Segment by using a pro rata valuation of the West End.

KJRY offers to pay \$3,393,363 (\$3,088,833 plus \$304,530), the alleged NLV of the Line, and to grant TP&W trackage rights over the Mapleton Segment to allow TP&W to serve its existing shippers for a trackage rights fee of \$2.50 per loaded or empty car. KJRY contends that its offer to pay the NLV satisfies the constitutional minimum standard. It claims that the West End has a negative GCV to TP&W allegedly because TP&W destroyed the value of the West End as a through route by diverting traffic to other routes and selling the last section, between La Harpe and Lomax, IL, to KJRY. See Keokuk Junction Railway Co.—Acquisition and Operation Exemption— West End of The Toledo, Peoria and Western Railway Corporation, STB Finance Docket No. 34143 (STB served Jan. 11, 2002). Additionally, KJRY states that TP&W: (1) has already attempted to sell and abandon the

² In December 2000, TP&W sold the operating easement over, and the rail, ties, and certain improvements on, the West End to SF&L Railway, Inc. (SF&L), a noncarrier. Subsequently, the Board determined that SF&L and its owners had abused the class exemption process by purchasing the West End with the intent to abandon and salvage it. The Board revoked the class exemption and ordered SF&L to reconvey its interest in the West End back to TP&W. SF&L Railway, Inc.—Acquisition and Operation Exemption—Toledo, Peoria and Western Railway Corporation, STB Finance Docket No. 33995 et al. (STB served Oct. 17, 2002 and aff'd with clarification Jan. 31, 2003) (SF&L Railway). The reconveyance occurred in February 2003.

³ KJRY's own in-house study assigned the West End an NLV of \$2,335,961. According to KJRY, the difference between its own valuation and the Gohmann valuation is attributable to differences in basic information and not methodology.

West End;⁴ (2) has effectively abandoned or embargoed the West End by raising rates to noncompetitive levels after having been forced to reacquire it in February 2003; and (3) plans to dispose of the West End, based on information disseminated from TP&W's corporate parent, RailAmerica, Inc.

KJRY contends that the Mapleton Segment is the only portion of the Line that TP&W regards as having value and that the proposed trackage rights would allow TP&W to retain its currently existing traffic on that segment. In effect, KJRY contends that TP&W would retain the GCV of the Line and that, as a result of the trackage rights, KJRY need not calculate a GCV. Accordingly, KJRY claims that its offer to pay the NLV of the Mapleton Segment of the Line also satisfies the constitutional minimum standard.

KJRY submitted 12 letters, 7 from shippers on the Line and 5 from overhead shippers that originate or terminate shipments on KJRY's own line,⁵ to demonstrate that rail service is inadequate for the majority of the Line's shippers. The letters claim that rail service via TP&W is no longer viable because of the noncompetitive rates TP&W is charging after having reacquired the West End.

KJRY contends that its acquisition of the Line will give TP&W cash and relieve it of an unwanted asset while preserving its access to the traffic-laden Mapleton Segment. KJRY claims that the acquisition will also result in improved transportation for the shippers that use the Line. KJRY says that it will bring new competitive service, new routes, and the advantages of a second carrier to shippers on the Mapleton Segment.

Constitutional minimum value. A feeder line application must contain "an estimate of the NLV and the GCV of the line and evidence in support of these estimates." See 49 CFR 1151.3(a)(4). KJRY's application failed to include an estimate of the Line's GCV and supporting evidence. As for the West End, however, a calculation of GCV is not required. The evidence KJRY presented here, the records compiled in SF&L Railway and SF&L Abandonment, and TP&W's own admission that "the Western Line does not generate sufficient traffic to cover its costs," TP&W Petition to reject at 14, n.8, are sufficient to demonstrate that the West End has a negative GCV. See, e.g., Sandusky County, et al.—Feeder Line Appl.—Conrail, 6 I.C.C.2d 568, 571 (1991) (calculation not required where record adequately demonstrates a negative GCV). Nor is the Board barred from limiting compensation to

⁴ In SF&L Railway, Inc.—Abandonment Exemption—in Hancock, McDonough, Fulton and Peoria Counties, IL, STB Docket No. AB-448 (Sub-No. 2X) (SF&L Abandonment), TP&W petitioned to substitute itself for SF&L in the latter's petition for an exemption to abandon the West End. The substitution request was denied.

⁵ KJRY owns and operates a 38-mile line of railroad between Keokuk, IA, and La Harpe.

NLV simply because a line will continue to be operated. See Chicago and North Western Transp. Co.—Abandonment, 363 I.C.C. 956 (1981) aff'd sub nom. Chicago and North Western Transp. Co. v. U.S., 678 F.2d 665 (7th Cir. 1982), and Amtrak—Conveyance of B&M in Conn. River Line in VT & NH, 4 I.C.C.2d 761, 781 (1988).

The same may not be said for KJRY's failure to submit a GCV estimate and supporting data for the Mapleton Segment.⁶ The Mapleton Segment has a significant GCV; it is served by TP&W 6 days a week and generates about 15% of TP&W's revenues. See TP&W Petition to reject, V.S. of Mr. Alfred Sauer. Nevertheless, KJRY wants the Board to force TP&W to sell the traffic-laden Mapleton Segment for its NLV, and in return KJRY would agree, subject to unspecified terms and conditions, to allow TP&W to continue serving currently existing shippers on its former line for a fee that allegedly is more than four times above the industry average.

KJRY's offer can only be viewed as a novel attempt to circumvent the statutory requirement intended to ensure that rail carriers receive nothing less than constitutional minimum value for rail lines acquired under the feeder line procedures. The failure to submit a GCV estimate and evidence on a line that clearly has a GCV makes it impossible to ensure compliance with 49 U.S.C. 10907(b)(1). KJRY's trackage rights offer is neither the equivalent of, nor a reasonable substitute for, an actual GCV estimate. As a result, KJRY's offer to purchase the Line for its NLV is deficient and subject to rejection to the extent it includes the Mapleton Segment.

Financial Responsibility. Even assuming that the Line is properly valued at \$3,393,363 and that the West End is properly valued at \$3,088,833, KJRY has not established that it has any financial resources of its own. Instead, it relies exclusively on Pioneer's financial resources. Mr. Guy L. Brenckman, President of both KJRY and Pioneer and Chief Executive Officer of the latter, claims that Pioneer has the necessary financial resources and that it is committed and able to fund KJRY's acquisition of the Line, but there is no agreement or commitment from Pioneer's Board of Directors to support KJRY's feeder line acquisition or what amounts to a personal commitment on Mr. Brenckman's part.

Pioneer claims that it can fund the purchase of the Line with \$5.7 million of available retained earnings and a \$1.1 million working capital line of credit from its principal bank, National City Bank of Peoria, IL (National City). An examination of Pioneer's balance sheet, however, shows that, for the year that ended on December 31, 2002, it had only \$1,148,461 in liquid assets and that its current liabilities exceeded its current assets by \$3,529,782 in 2001 and by \$1,064,514 in 2002. Pioneer also claims that it can fund the rehabilitation and operation of the Line from its \$1.1 million working capital

⁶ While KJRY seeks discovery on all movements originating or terminating on the Mapleton Segment, its application does not rely on GCV.

line of credit and from income from operations. Pioneer's income statement for 2002 shows \$1,245,689 in net income from operations. Pioneer, however, has failed to submit detailed operating plans and pro forma financial statements for the first 3 years KJRY would operate the Line.⁷

In addition to retained earnings, Pioneer claims that National City has already expressed interest in providing financing. An April 3, 2003 letter from National City to Mr. J. Michael Carr, KJRY's and Pioneer's Chief Financial Officer, states that National City "would be pleased to consider additional financing up to \$5 million subject to our normal and satisfactory due diligence procedures." KJRY Application at 113 (V.S. of Carr, Exhibit B). In its May 7, 2003 reply, Pioneer states that the loan officer at National City is recommending that the bank's loan committee approve a loan of up to \$5 million to be used for the acquisition and working capital but that the loan committee is not scheduled to meet until May 13, 2003. Expressions of interest and loan assurances, however, do not constitute a loan commitment for the purchase of the Line. See, e.g., Wisconsin & Michigan Railway Company—Feeder Line Application—Wisconsin Central, Ltd., Finance Docket No. 31939 (ICC served Dec. 6, 1991) (Wisconsin & Michigan) at 3, and KC Railway—Feeder Line Application—Union Pacific Railroad in Kansas and Colorado, Finance Docket No. 31926 (ICC served Sept. 3, 1991) at 1.

Pioneer also claims that in a matter of weeks it can raise \$1.5 to \$2 million by selling security interests in its operating equipment. Whether or not this assertion is accurate, it still does not constitute a loan commitment. Pioneer has failed to demonstrate either a loan commitment or adequate resources of its own to finance the purchase of, and to operate for the initial 3-year period, either the Line or the West End.

In summary, KJRY has failed to establish that it is a financially responsible person able to pay the NLV of either the Line or the West End or to cover the expenses associated with providing rail service over either of them for the first 3 years of operation. As a result, KJRY has not demonstrated that it is financially responsible.

KJRY's application is subject to rejection based on the above deficiencies. Nevertheless, Board policy encourages feeder line applications.⁸ Accordingly, it is appropriate for KJRY to submit,

⁷ In its May 7, 2002 reply, KJRY submitted a 1-year operating statement and traffic projection for the West End.

⁸ Wisconsin & Michigan (ICC served Oct. 9, 1991), at 2 (citing Kansas City Southern Railway Company—Feeder Line Application—Atchison, Topeka and Santa Fe Railway Company, Finance Docket No. 31823 (ICC served July 9, 1991), and Revision of Feeder Railroad Development (continued...)

within 30 days from the service date of this decision either: (1) a GCV estimate along with supporting data for the Mapleton Segment of the Line, additional evidence of financial responsibility to purchase and operate the entire Line, and more detailed operating plans and pro forma financial statements; or (2) evidence of financial responsibility to purchase and operate only the West End and more detailed operating plans and pro forma financial statements. Alternatively, KJRY may file a revised application correcting the above deficiencies and incorporating portions of the instant application by reference. See 49 CFR 1151.2(b)(2).

This decision should not be read as taking a position on KJRY's argument that, under Caddo Antoine and Little Missouri R. Co. v. U.S., 95 F.3d 740 (8th Cir. 1996), all of the track at issue here must be considered an "entire line" within the meaning of that decision.

This decision will not significantly affect either the quality of the human environment or the conservation of energy resources.

It is ordered:

1. The application or the portion of the application that includes the Mapleton Segment will be rejected and the proceeding or the portion of the proceeding that includes the Mapleton Segment will be discontinued if KJRY does not submit, within 30 days from the service date of this decision, the information discussed above.

2. This decision is effective on the date of service.

By the Board, David M. Konschnik, Director, Office of Proceedings.

Vernon A. Williams
Secretary

⁸(...continued)
Rules, 7 I.C.C.2d 902 (1991)).